

Before The
SURFACE TRANSPORTATION BOARD

STB EX PARTE NO. 661

RAIL FUEL SURCHARGES

COMMENTS OF
The HONORABLE BRIAN SCHWEITZER
GOVERNOR OF MONTANA

I. INTRODUCTION

Mr. Chairman, Vice Chairman Mulvey and staff of the Board, I thank you for the opportunity and welcome the chance to present comments on railroad fuel surcharges in this hearing. I stand before you not only as the Governor of Montana, but as a farm producer, a businessman and most importantly as a citizen who has many years of experience dealing with our railroad problems in Montana.

I could have come here with big fancy consultants and high priced lawyers and ‘converse’ with you about esoteric issues that only an attorney would understand. Instead, I came here personally to demonstrate my concern for the lack of focus and energy past Boards have shown about the continuing plight of American industry and the rising monopoly power being exerted by the railroads.

I want to personally thank Chairman Buttrey for his recent visits out to Montana to view for himself some of the problems we are facing with the single market dominated railroad system. You, Mr. Chairman, Vice Chair Mulvey and any of the Board staff are welcome to come to Montana at my personal invitation – we are great tour guides, and we have lots of railroad problems to show you.

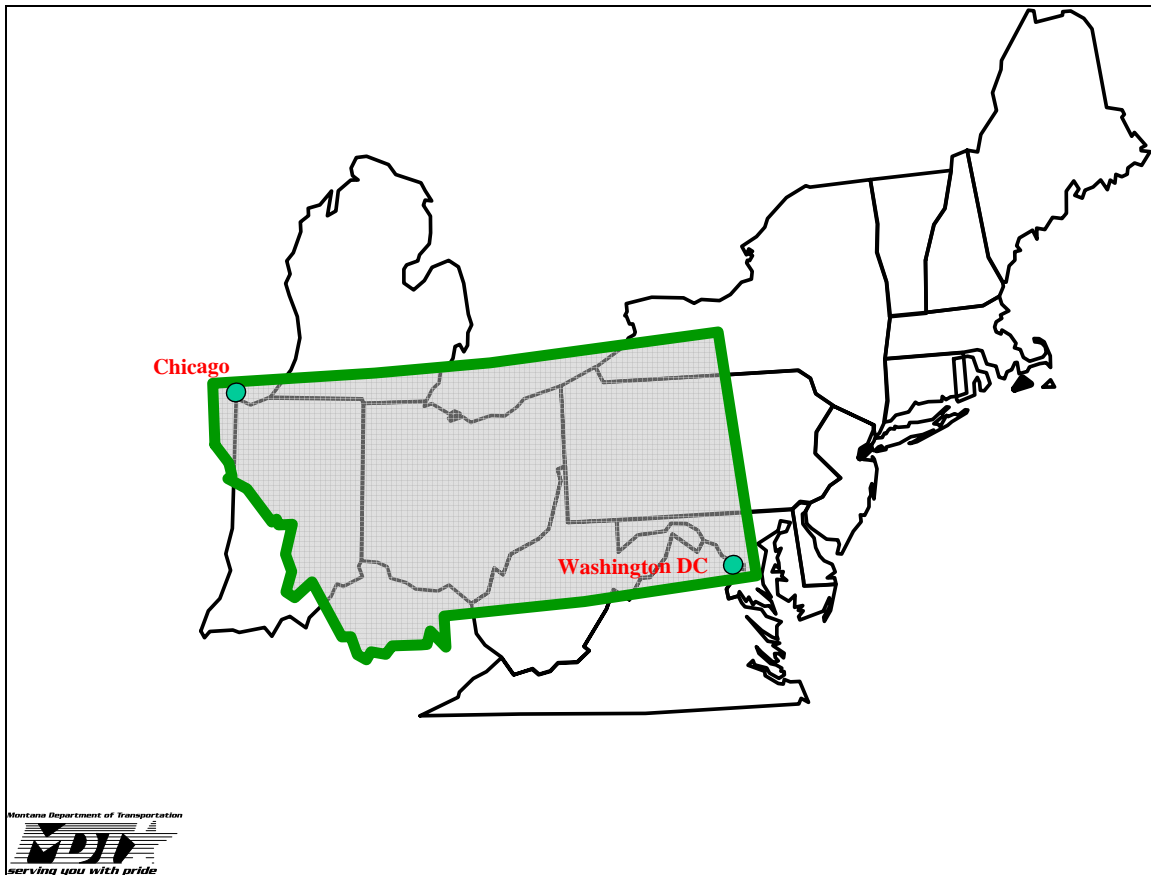
The state of the railroad situation in Montana can best be titled: A Spirit of Hope and a Story of Survival.

Montana ranks third among the states in all wheat production. More specifically, it ranks 3rd in spring wheat production and 2nd in durum production. Montana also ranks 3rd in barley production, 3rd in lentils production, 3rd in dry edible peas production, 2nd in Austrian pea production, and 2nd in flax production. Montana originated over 37 million tons of rail traffic, which ranks it 17th in the nation. At the same time Montana bridged over 78,000,000 tons of rail traffic.

Our spirit of hope is buoyed by the fact that things cannot get much worse, and Montanans are a tough people who will seek and find solutions to their most vexing problems. Our story of survival is centered around the fact that this Board and its predecessor, the Interstate Commerce Commission, have allowed the creation of a monopoly in Montana in a land where the goods we produce are mostly bulk commodities requiring movement by rail to points outside of Montana.

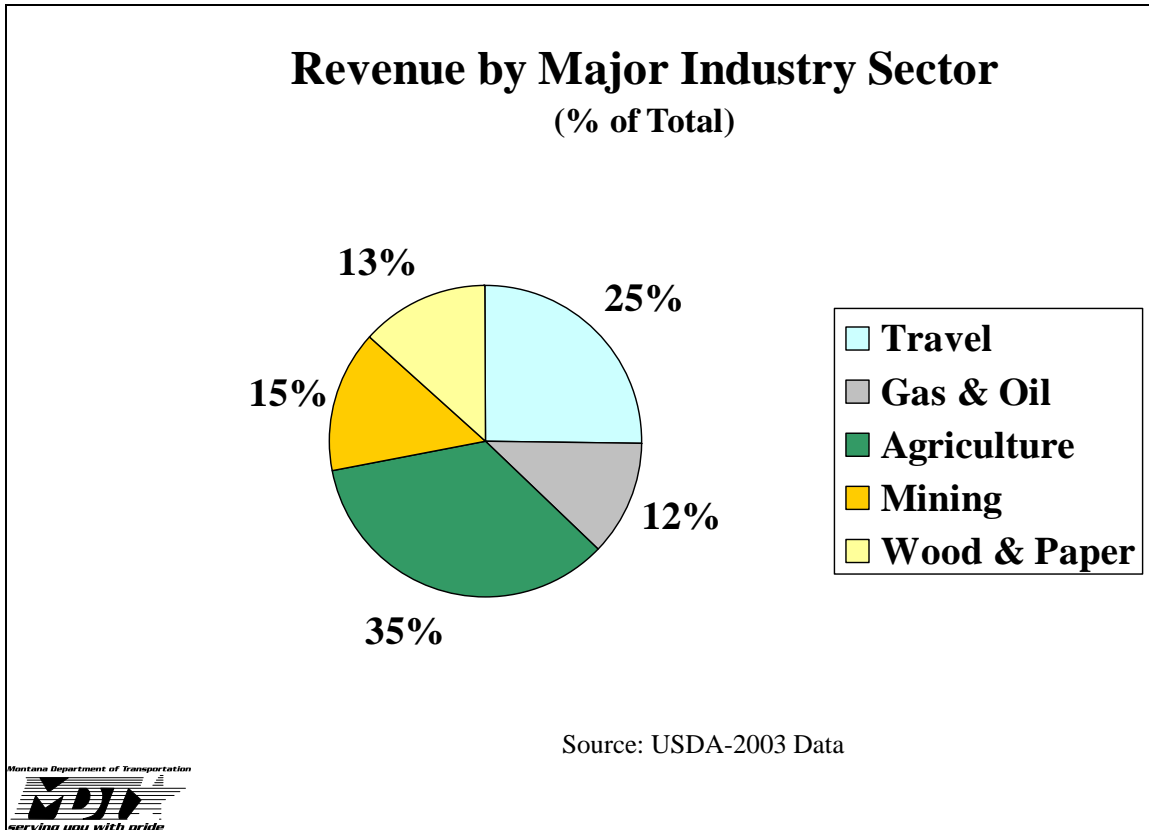
Montana is dominated by a single railroad, the BNSF, which controls 94% of the Montana rail system. This makes Montana the #1 rail-dominated state in country. After Montana at 94% is Delaware at 83%, followed by Idaho at 80%, North Dakota at 66%, and South Dakota at 54%. The BNSF controls over 91% of the actual tonnage hauled out of Montana and 92% of the rail revenue generated in the state. Since 1975, Montana has seen over 1,900 miles of rail line abandoned (over 37% of the rail miles) because there is no rail-to-rail competition. And the distances are

large—very, very large. To put this vastness in perspective, if one were to place one corner of Montana over Washington DC, the other corner would cover Chicago, IL.



Montana's top four industrial activities are agriculture, tourism, mining and lumber. Montana's economy and wealth is thus highly dependent upon the production and shipment of commodities. In order for these commodities to have value to Montanans, they must be shipped to points outside the state or country to market. It is this absolute reliance upon good, affordable, and efficient transportation that brings me to this hearing today. We hope for a better day, where fairness in regulation and

more rail competition will rule the land. Meanwhile, we struggle every day trying to survive under monopoly domination.



Here is the mathematical formula we deal with every day in Montana: *Large Land Area + Low Population + Lack of Large Internal Markets + Long Distance From Markets + Raw Commodity Economy = Heavy Reliance on Rail.*

Our Montana concerns are founded on four points:

1. Rail transportation is vitally important to Montana's raw commodity-based economy
2. Montana's rail system increasingly serves simply as a bridge for long-distance traffic.
3. Increasing numbers of short lines and abandonments have reduced Montana shipper access to Class I rail service
4. Dominance of one Class I railroad continues as #1 freight issue in Montana

Shippers used to take cases to the Surface Transportation Board expecting to get fair and balanced treatment, but shippers haven't found any relief at the STB for a long, long time. They have instead become so discouraged by the precedents of the past few years that only a very few have the funds, or the confidence, to bring a case. Faced with the effects of a railroad monopoly that was withering away a key element of the state's economy, Montana in 1980 filed a class-action and formal complaint. We pursued the *McCarty Farms* case for **17 years**. In this case the *ICC on December 14, 1984 found that the BN had market dominance and that its rates were unreasonable*. The Administrative Law Judge (ALJ) further found that the rates were higher than 300% of variable cost! The State of Montana spent \$3.2 million, yet this Board in 1997 found that these rates were not excessive! This Board ruled against the farm producers of Montana after changing the regulatory standards twice.

Regulatory oversight of the railroads, or lack of it, affects everything we do in Montana, every day.

Montanans bear the freight charges on commodities produced in Montana. We have no choice.

You may not want to hear it, but from where we stand, this Board—with its past actions and those of the former Interstate Commerce Commission—created the ‘railroad mess’ we have out west and in Montana, and have done little to help us fix it. We didn’t want a single monopoly railroad controlling our state. We stated that over and over in the hearings that preceded the creation of the Burlington Northern. But your predecessors made it happen when they allowed the three major transcontinental railroads that crossed Montana to form a single company in Burlington Northern. Montana went from FOUR healthy transcontinental railroads in 1970 to one today that dominates the entire state. Then, when the Milwaukee Road (the ICC’s designated competitor for the BN) failed just 9 years later, no one from this Board or the ICC came back out to Montana to clean up the monopoly mess they had created. We live with it everyday.

I am here to tell you that we are tired of paying more than our fair share. We, in Montana, are supportive of fair treatment for all rail shippers. We are tired of being abused by poor service. We are tired of having the monopoly railroad service only rail lines they want to service and not fix railroad lines important to the citizens of Montana and even though they are still in service. Instead, they use the rail lines in Montana to ‘hide from the tax man’ by storing thousands of cars on light density lines.

They are unable to service the customers on those blocked lines and later use this lack of service as grounds for abandonments. Chairman Buttrey, in his last visit to my State, saw this firsthand, and heard directly from the people of Montana about their struggles with the railroads.

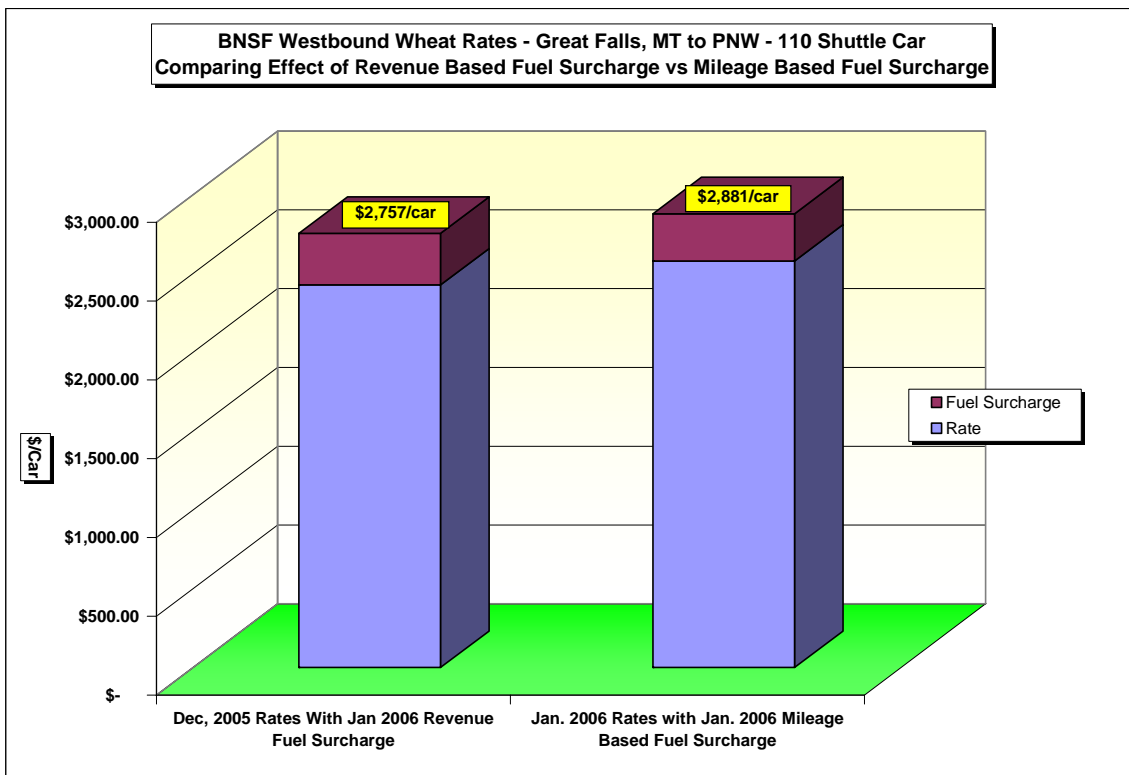
I realize that you, at the Board, will see in these remarks, areas that are not germane to the proceeding at hand. But you also have to realize it is not every day that a governor gets a chance to talk to you in your chambers, and these issues are very much germane to Montanans.

The fuel surcharge issue is a perfect example of what has gone awry with the monopoly railroads. In Montana we pay some of the highest freight rates in the nation regardless of distance. Why? Lack of rail-to-rail competition. In Montana the car shortages start early and last longer. Why? Lack of rail-to-rail competition.

When the BNSF and UP introduced the concept of fuel surcharges several years ago, they based their 'fuel surcharges' on rate levels. Thus those who were the most captive, who had and paid the highest rates, paid the most fuel surcharge. Montanans tired of paying more than our fair share. That is an unreasonable carrier practice.

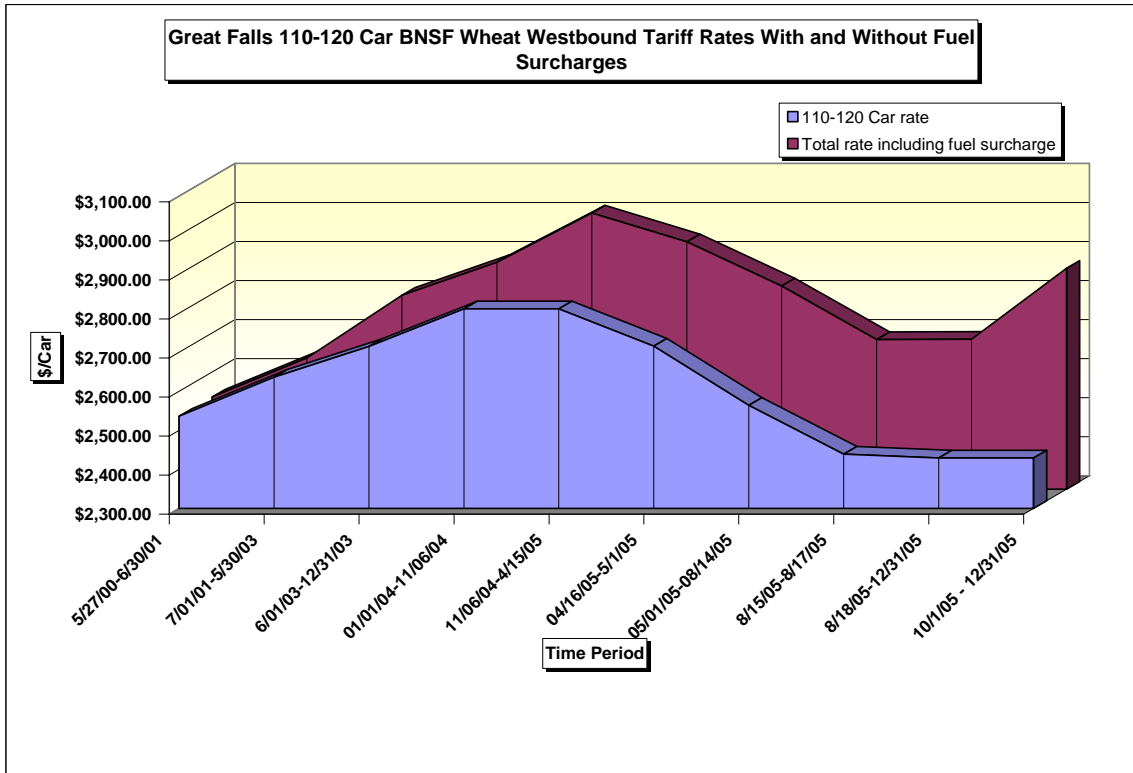
After a great deal of rhetoric exchange with the BNSF railroad over a number of years, BNSF announced that for direct shipments from Montana on wheat and bar-

ley there would be a mileage-based fuel surcharge program because it would be inherently fairer to those with elevated rate levels. This amounted to recognition by the BNSF that rate based surcharges are an unfair rate practice. My transportation advisors told me before we saw the 'devil in the details' from the BNSF, that Montana would be paying MORE after a switch to mileage-based fuel surcharges than they were under 'revenue-based' fuel surcharge. And you know what – they were right. Today, Montana rail rates are just as high or higher with mileage-based fuel surcharges than they were under 'revenue-based' fuel surcharges. Why? Because the BNSF simply raised the underlying rates and then applied a slightly smaller mileage-based fuel surcharge than the revenue-based fuel surcharge. Thus the BNSF is again making more money while we in Montana are again subsidizing the rest of the rail shippers and railroads in this country. Yes, the BNSF has stated that the mileage-based fuel surcharge would collect essentially the same amount of surcharge as revenue-based programs. In areas such as Montana where the rate levels are among the highest in the nation, the switch to mileage based fuel surcharge in Montana should show substantial relief from excessive rate-based fuel surcharge. The switch resulted in higher rates, and that makes my point and shows how the railroads continue to over-collect from Montanans.



We hear over and over from the BNSF and AAR that the railroad rates in Montana are actually going down.

I want you at the Board to understand that the truth is that the transportation rates we pay include all of the charges, transportation to the elevator, handling, rail rate and fuel surcharges, and all of those charges continue to go up and up and up.



Now we are hearing that BNSF is receiving so much flak from more distant shippers (where there is rail competition) that BNSF is contemplating modifying and reducing the effect of the mileage-based fuel surcharge on those shippers, but not in areas like Montana where they have a monopoly. Again, Montanans are paying more than our fair share. We are darn tired of that.

It is my view that when the Staggers Rail Act of 1980 was passed, Congress was seeking two major outcomes. By focusing on deregulation, the charge was to:

- 1) produce a stronger rail industry than the one that was, at that time, plagued with multiple bankruptcies, and
- 2) be protective of the captive rail customers from potential abuse that might occur due to decreased regulatory oversight and the inevitable

consolidations that would occur in the future. There is a call for balance in this bill from Congress.

Chairman Buttrey and I have visited at length about this—increased rail-to-rail competition was called for by Congress in the 1980 Staggers Rail Act. In Title 49, Subtitle IV, Part A, Chapter 101: Section 10101—Rail Transportation Policy, the word ‘competition’ is utilized in four of the fifteen parts:

1. to allow, to the maximum extent possible, competition and the demand for services to establish reasonable rates for transportation by rail;
4. to ensure the development and continuation of a sound rail transportation system with effective competition among rail carriers and with other modes, to meet the needs of the public and the national defense;
5. to foster sound economic conditions in transportation and to ensure effective competition and coordination between rail carriers and other modes;
6. to maintain reasonable rates where there is an absence of effective competition and where rail rates provide revenues which exceed the amount necessary to maintain the rail system and to attract capital

Fuel Surcharge Issues

The most pressing question, and the heart of this Ex Parte exploration, is what is best to address the public interest. After all, protecting the public interest is clearly what Congress desires when it makes changes to the regulatory scheme. In our mind, the rail customer—the public—needs a competitive rail transportation system that provides fairly priced, safe and reliable service.

Are fuel surcharges that recover more than the system-wide fuel cost increases incurred by a railroad a reasonable carrier practice? Clearly, no.

Are fuel surcharges that recover more fuel surcharge for a particular movement than is incurred by a railroad a reasonable carrier practice? Clearly, no.

Are fuel surcharges that are levied on only part of the rail shippers at levels that return all—or more than all—of the fuel price increases for the whole railroad system a reasonable carrier practice? Clearly, no.

Are fuel surcharges levied on Montana rail shippers—who have no alternative other than rail movement—that compensate the railroad for the lack of fuel surcharges on other rail movements a reasonable carrier practice? Clearly, no.

One shipper should not be charged more than the actual fuel allocated to the movement of their goods.

The BNSF's 4th Quarter 2005 price for fuel was \$1.69/gallon. At the same time, in December of 2005, they were assessing an 18.5% fuel surcharge on movements from Montana. On a movement from Great Falls, Montana to the Pacific Northwest (PNW) in \$ /car, the rate was \$3,029 (single car). My costing experts tell me that the estimated fuel cost on BNSF for each Gross Ton Mile/gal is 758 (based

upon published, 4th Q 2005), so for a 882 mile haul the estimated fuel cost would be about \$315.60/car. Yet the BNSF was collecting 18.5% fuel surcharge based upon rate (\$560.36/car), which is a Surcharge Revenue/Fuel Cost ratio of 1.78. The BNSF was and continues to assess fuel surcharge that are greater than actual fuel costs on the movements from Montana, even under the mileage-based fuel surcharge system—an unfair rate practice. Remember that when the BNSF in January, 2006 changed to mileage-based fuel surcharges for these same Montana movements, our rates actually increased again.

Montanans need fairness in pricing by the railroads. They should not have to continue to bear more than their fair share. That is why this Board exists—to bring fairness of practice to a market dominated by monopoly/duopoly rail industry.

IV. CONCLUSION

Broad change is needed. The railroad needs to price fairly. I am hopeful you will find that the way fuel surcharges are being implemented is the unfair rate practice that it is, and that you will open a rule-making proceeding to instill fairness in the marketplace.

I also fervently hope that we will see a new day at this Board, with you, Chairman Buttrey and Vice Chairman Mulvey, initiating the more balanced approach that was called for by Congress in the 1980 Staggers Rail Act.

Respectfully submitted,

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